LEGISLATIVE SERVICES AGENCY

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FISCAL IMPACT STATEMENT

LS 6974
BILL NUMBER: SB 483

NOTE PREPARED: Jan 30, 2013
BILL AMENDED:

SUBJECT: Administration of County Income Taxes.

FIRST AUTHOR: Sen. Kruse
FIRST SPONSOR:

BILL STATUS: As Introduced

FUNDS AFFECTED: X GENERAL
DEDICATED
FEDERAL

IMPACT: State & Local

Summary of Legislation: This bill provides that beginning January 1, 2014, the Department of State Revenue (DOR) will no longer collect and administer local option income taxes (LOIT). The bill repeals provisions related to: (1) the state collection of LOIT; and (2) the calculation and distribution by the state of certified distributions of LOIT revenue.

Counties who impose a LOIT will have the authority and responsibility for the administration, collection, and enforcement of their income tax. The bill provides that LOIT withholdings should be remitted directly to the county treasurer of the county that imposed the tax. It requires taxpayers to file LOIT returns and to remit the tax due to the county treasurer of the county that imposed the tax. The county treasurer will issue refunds if a taxpayer's payments exceed their LOIT liability. The bill specifies that certain provisions related to the DOR's administration of state taxes also apply to a county administering a LOIT.

Effective Date: Upon passage; January 1, 2014.

Explanation of State Expenditures: *LOIT Account Balances:* While the bill requires the state to transfer to each county the balance in its LOIT account and abolish those accounts before January 15, 2014, it does not provide for the state to recover funds from counties that have negative LOIT account balances at that time. It is unclear whether the counties would or would not have to pay those funds back to the state. A total of 33 counties had negative LOIT account balances as of the December 31, 2011, ending balances adjusted for the special LOIT distributions that were made on April 5, 2012. These negative LOIT account balances total approximately $105.7 M. The potential negative balances that may exist as of December 31, 2013, are unknown.

Department of State Revenue (DOR): This bill transfers the administration and collection of LOIT from the DOR to the counties that impose LOIT. (Note: LOIT includes CAGIT, COIT, CEDIT, LOIT for property tax freeze, LOIT for property tax relief, and LOIT for public safety.) Currently, the DOR collects and administers LOIT for 91 counties. Only Lake County does not impose LOIT. The DOR will be able to reallocate dedicated staff to other functions. However, the cost savings from transferring LOIT collection and administration to the counties will likely be small because the DOR will still collect the state Individual Adjusted Gross Income Tax which is imposed on the same population.

State Budget Agency (SBA): The SBA will no longer be required to calculate the certified distributions of LOIT revenue. In addition, the SBA will no longer be required to produce all the reports associated with the collection and accounting of LOIT revenue. Staff and resources dedicated to these functions will be allocated to different tasks.

Explanation of State Revenues:

Summary of NET Local Impact: The net impact of this bill will vary by county.

(1) The bill makes the collection and administration of LOIT the responsibility of the counties that impose LOIT. Counties will have to dedicate and expend resources to collect LOIT revenue and to administer the tax. This will increase the overall operating costs of county governments. Currently, LOIT is administered by the state at no cost to the counties.

(2) The bill also eliminates the certified distribution process currently in place. The certified distribution process provides LOIT revenue collected by the state back to the counties. The certified distribution for a county in a particular calendar year is based on tax returns two years prior. By eliminating the certified distribution process, counties will begin to receive money directly from taxpayers. In the long run, revenue from current year direct collection should be equivalent to revenue that counties would receive under the current system.

(3) The bill requires the state to transfer the remaining balances in the county LOIT accounts before January 15, 2014. This one-time payment may offset the initial costs to begin administering LOIT in counties that have a LOIT account balance at that time.

Explanation of Local Expenditures: *Summary* - This bill provides counties with the authority and responsibility to collect and administer LOIT. Currently, 91 counties impose LOIT. Lake County is the only county that does not impose LOIT. Under the bill, counties will either have to collect and administer LOIT or enter into a contract to provide the necessary services. This will increase the administrative expenses of the counties imposing LOIT, requiring the staff and resources necessary to collect withholding payments from employers, collect quarterly estimated payments from taxpayers, process annual returns from taxpayers, issue refunds and assessments, and perform compliance activities. Since the counties have not previously administered an income tax, they will likely need to acquire additional resources to administer LOIT. The initial start-up costs will vary depending on each county's current resources and the administrative functions that counties conduct that can be adapted to income tax administration. For some counties, the initial expenditures for staff and resources could be significant. Once the appropriate resources are in place, the the annual collection cost as a percent of revenue is estimated to be between 1.7% to 2.2% ,with a minimum cost estimated at $270,000 annually. Currently, the state bears all cost of collecting and administering LOIT for the counties. The table at the end of the document contains the estimated county collection cost.

Additional Information - This bill moves the collection and administration of LOIT from the DOR to each county that imposes LOIT. The bill requires the county treasurers to collect and administer:

- Estimated payments of LOIT from county taxpayers.
- Remittance by employers of LOIT withheld from employee wages.
- LOIT paid by taxpayers with annual tax returns.

The bill states that employers must remit wages withheld for LOIT purposes to the appropriate county treasurer. For example, if an Allen County business employed people living in Dekalb County, Adams County, and Allen County the business would have to remit the correct withholding amounts to the counties where the employees reside. The bill requires the county to receive the employer and employee withholding statements necessary to process LOIT returns and compute LOIT liabilities.

The bill states that county taxpayers will file their LOIT return with their county treasurer. The county treasurer must be able to provide the taxpayers with an appropriate form to fulfill this filing obligation. The county is required to process the return and any payment that was sent with it. If the taxpayer is due a refund, the county treasurer is required to issue it.

The county treasurers are required to administer LOIT as it exists in current law. In addition, the county treasurers will be held to similar standards as the DOR. For example, the county treasurers are subject to the same timing parameters regarding refunds and interest. The bill requires county treasurers to retain records of all tax returns and payments received for at least three years. There are three operational exceptions listed in the bill:

- Paid preparers are not required to file LOIT returns electronically with the county treasurers.
- Employers are not required to electronically remit withholding information and payments to the county treasurers.
- County treasurers are not required to cross check employer WH-3 withholding returns to individual W-2 forms.

The county treasurers are granted the authority to perform the tasks necessary to administer LOIT including enforcement powers. They will be able to issue assessments, employ collection techniques, operate audit programs, and levy penalties. The responsibilities are the same as under current statute, but must be implemented by county treasurers and not the DOR.

Each county treasurer's office will incur additional expenses to administer LOIT. First, county treasurers may have initial expenses to acquire additional IT resources, print forms, notify employers across the state regarding withholding, and develop returns processing systems. Because of the confidential information contained on an income tax return, county treasurers likely will have to implement new security protocols. In addition, county treasurers will likely receive federal income tax information, so they will have to become compliant with the Internal Revenue Service (IRS) data integrity rules. After all the resources are in place, the annual collection cost as a percent of revenue is estimated to be between 1.7% to 2.2% with a minimum cost of $270,000 annually.

The collection cost as a percent of revenue (collection cost ratio) will likely vary for each county. Due to economies of scale, the larger the tax base combined with efficient use of technology, will decrease the collection cost ratio. For example, the DOR has a collections cost ratio of approximately 0.43%. While the IRS has a collections cost ratio of about 0.5%. The estimated collections costs for the county treasurers is based on the collection costs of municipalities in other states that administer a local income tax.

Explanation of Local Revenues: *LOIT Collections:* Currently, LOIT is distributed by the state based on the certified distribution process performed by the State Budget Agency. The majority of the certified distribution for a particular calendar year is based on tax returns filed for a taxable year two years prior. As a result, there is a lag between the actual revenue collected from LOIT by the DOR and the basis of the LOIT certified distribution for a county. This bill eliminates the certified distribution process as of January 1, 2014. After January 1, 2014, counties will collect LOIT on a current year basis through withholding payments by employers, quarterly estimated payments from taxpayers, and payments made with annual returns. Currently, a county's certified distribution for CY 2014 would be based on the returns processed in FY 2013, 95% of which would be for taxable year 2012 and the balance tax year 2011. Under the bill, counties would receive taxes actually paid in tax year 2014. While collections in 2014 may deviate from the amounts a county otherwise may have received under the certified distribution process, it is expected that revenue counties will receive in the long run under the bill will be equivalent to what they would receive under the current system.

LOIT Account Balances: The bill requires the state to transfer to each county the balance in its LOIT account and abolish those accounts before January 15, 2014. A total of 58 counties had balances in their LOIT accounts based on their December 31, 2011, ending balances adjusted for the special LOIT distributions that were made on April 5, 2012. These LOIT account balances total approximately $83.3 M. The potential balances that may exist as of December 31, 2013, are unknown.

State Agencies Affected: Department of State Revenue; State Budget Agency.

Local Agencies Affected: Counties with a local option income tax.

Information Sources: DOR *Agency Operating Account Summary,* 2012; DOR, *Budget Committee Hearing Presentation,* 2012; City of Sidney Budget, *Proposed 2012 Budget*; City of Battle Creek, *Preliminary Budget: Fiscal Year 2012-2013*; IRS, *FY 2012 Budget Request*; LSA - LOIT: 1% Estimates of Certified Distributions; SBA, *Local Option Income Tax Balance Report Through 2010 Actual and 2011 Estimated August 2012,* August 3, 2012.

Fiscal Analyst: Heath Holloway, 317-232-9867.

County	Collection & Admin. Costs		County	Collection & Admin. Costs	
	CY 2014	CY 2015		CY 2014	CY 2015
Adams	($270,000)	($270,000)	Madison	($523,000)	($536,000)
Allen	($1,995,000)	($2,033,000)	Marion	($4,330,000)	($4,424,000)
Bartholomew	($483,000)	($493,000)	Marshall	($270,000)	($270,000)
Benton	($270,000)	($270,000)	Martin	($270,000)	($270,000)
Blackford	($270,000)	($270,000)	Miami	($270,000)	($270,000)
Boone	($574,000)	($594,000)	Monroe	($662,000)	($679,000)
Brown	($270,000)	($270,000)	Montgomery	($270,000)	($270,000)
Carroll	($270,000)	($270,000)	Morgan	($362,000)	($371,000)
Cass	($270,000)	($270,000)	Newton	($270,000)	($270,000)
Clark	($549,000)	($560,000)	Noble	($270,000)	($270,000)
Clay	($270,000)	($270,000)	Ohio	($270,000)	($270,000)
Clinton	($270,000)	($270,000)	Orange	($270,000)	($270,000)
Crawford	($270,000)	($270,000)	Owen	($270,000)	($270,000)
Daviess	($270,000)	($270,000)	Parke	($270,000)	($270,000)
Dearborn	($274,000)	($278,000)	Perry	($270,000)	($270,000)
Decatur	($270,000)	($270,000)	Pike	($270,000)	($270,000)
DeKalb	($270,000)	($270,000)	Porter	($1,167,000)	($1,205,000)
Delaware	($437,000)	($445,000)	Posey	($270,000)	($270,000)
Dubois	($300,000)	($308,000)	Pulaski	($270,000)	($270,000)
Elkhart	($773,000)	($786,000)	Putnam	($270,000)	($270,000)
Fayette	($270,000)	($270,000)	Randolph	($270,000)	($270,000)
Floyd	($446,000)	($449,000)	Ripley	($270,000)	($270,000)
Fountain	($270,000)	($270,000)	Rush	($270,000)	($270,000)
Franklin	($270,000)	($270,000)	St. Joseph	($1,293,000)	($1,319,000)
Fulton	($270,000)	($270,000)	Scott	($270,000)	($270,000)
Gibson	($270,000)	($270,000)	Shelby	($270,000)	($270,000)
Grant	($270,000)	($270,000)	Spencer	($270,000)	($270,000)

County	Collection & Admin. Costs		County	Collection & Admin. Costs	
	CY 2014	CY 2015		CY 2014	CY 2015
Greene	($270,000)	($270,000)	Starke	($270,000)	($270,000)
Hamilton	($3,130,000)	($3,325,000)	Steuben	($270,000)	($270,000)
Hancock	($454,000)	($468,000)	Sullivan	($270,000)	($270,000)
Harrison	($270,000)	($270,000)	Switzerland	($270,000)	($270,000)
Hendricks	($1,029,000)	($1,081,000)	Tippecanoe	($824,000)	($841,000)
Henry	($270,000)	($270,000)	Tipton	($270,000)	($270,000)
Howard	($368,000)	($373,000)	Union	($270,000)	($270,000)
Huntington	($270,000)	($270,000)	Vanderburgh	($879,000)	($894,000)
Jackson	($270,000)	($270,000)	Vermillion	($270,000)	($270,000)
Jasper	($270,000)	($270,000)	Vigo	($444,000)	($449,000)
Jay	($270,000)	($270,000)	Wabash	($270,000)	($270,000)
Jefferson	($270,000)	($270,000)	Warren	($270,000)	($270,000)
Jennings	($270,000)	($270,000)	Warrick	($442,000)	($458,000)
Johnson	($897,000)	($929,000)	Washington	($270,000)	($270,000)
Knox	($270,000)	($270,000)	Wayne	($270,000)	($270,000)
Kosciusko	($378,000)	($385,000)	Wells	($270,000)	($270,000)
Lagrange	($270,000)	($270,000)	White	($270,000)	($270,000)
LaPorte	($512,000)	($523,000)	Whitley	($270,000)	($270,000)
Lawrence	($270,000)	($270,000)			